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No. 87-1382

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

v.

MAUREEN A. STAPLES AND MICHAEL P. STAPLES,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

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BRIEF FOR THE RESPONDENTS

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QUESTIONS PRESENTED

I. Whether the Internal Revenue Service incorrectly interpreted Section 170 of the Internal Revenue Code of 1954 in reversing seven decades of prior IRS policy and disallowing charitable contribution deductions for payments made by individual Scientologists solely to participate in religious services of their faith.

II. Whether denying charitable contribution deductions under Section 170 for payments to participate in their faith's religious sacraments by Scientologists violates the religion clauses of the First Amendment.

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BRIEF FOR THE RESPONDENTS

OPINIONS BELOW

The opinion of the Court of Appeals (Pet. App. 1a-9a) is reported at 821 F.2d 1324. The order and decision of the Tax Court in the case designated by the parties as providing factual and legal findings in this case is reported as *Graham v. Commissioner*, 83 T.C. 575 (1984) (Pet. App. 12a-22a).[1] The order of the Tax Court in this case is unreported (Pet. App. 11a),

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[1] References in this brief are indicated as follows:

To the numbered pages of the Appendix filed with the government's petition in this Court (Pet. App. ——a); To the

JURISDICTION

The judgment of the court of appeals was entered on July 1, 1987. A petition for rehearing was denied on September 24, 1987 (Pet. App. 10a). On December 12, 1987, Justice Blackmun extended the time within which to file a petition for a writ of certiorari to and including February 20, 1988, and the petition was filed on February 19, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The religion clauses of the First Amendment to the United States Constitution and pertinent portions of 26 U.S.C. § 170 and 26 U.S.C. § 501 are set forth in the Appendix to this brief (12a).

STATEMENT OF THE CASE

Petitioner, the Commissioner of Internal Revenue (the "Commissioner"), denied respondents, Maureen and Michael Staples, an income tax deduction of $2,928 for payments to their church, the Church of Scientology, made solely to participate in the central religious practices of their faith. Disallowance of these deductions produced a tax deficiency of $302.80 (Add. 7). Respondents filed a petition in the Tax Court for review of the Commissioner's determination and, along with hundreds of similarly situated Tax Court petitioners who had contributed sums of money to various churches and missions of the same religious denomination, waived trial and, subject to their right of appeal, agreed to be bound by the outcome of similar "test cases." The Commissioner

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numbered pages of the Appendix to this brief (——a); To the volume number and numbered pages of a four-volume Stipulated Record on Appeal filed in the court below (Stip. Rec. ——); To the Required Addendum filed with respondents' main brief in the court below (Add. ——).

and the respondents stipulated in the Tax Court that such designated cases were typical and that, to the extent relevant, the record of those cases was to be incorporated into the record of all proceedings in respondents' case.

The Tax Court ruled in favor of the Commissioner in the test case *Graham v. Commissioner*, 83 T.C. 575 (1984), and on the authority of that decision entered its judgment in favor of the Commissioner in respondents' Tax Court case. Respondents then filed a timely notice of appeal from the Tax Court's decision and appealed to the United States Court of Appeals for the Eighth Circuit which reversed the decision of the Tax Court. *Staples v. Commissioner*, 821 F.2d 1324 (8th Cir. 1987) (Pet. App. 1a).

The payments at issue in this case were made for the core religious practice of the Church of Scientology known as "Auditing." Specifically, the record, through the detailed stipulations of fact, established that parishioners of Scientology are taught that "the individual is an immortal spirit who has a mind and a body" and "that the highest level of spiritual ability and awareness can be obtained only by progressing on a step-by-step basis through lower and intermediate levels of Auditing." (3a, ¶ 16).[2] "Every Auditing session is structured and conducted in exact accordance with rituals, codes, doctrines and tenets of Scientology" (3a, ¶ 15). No subject matter is taught, studied or learned during auditing. (4a, ¶ 23). Dr. Thomas Love, a professor of religious studies at California State University at Northridge, California, gave his uncontradicted expert opinion that "auditing," the service for which the bulk of contributions involved were made, is "the essential religious

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[2] The parties' stipulations in *Graham v. Commissioner*, incorporated by reference in the proceedings below, are reprinted in the Appendix to this brief (1a).

experience of the Church of Scientology." (Stip. Rec. III 390-396).

The Church of Scientology engages in another religious practice also at issue here known to Scientologists as "training." In training parishioners study "the doctrines, tenets, codes, policies and practices of Scientology" (4a, ¶ 24), and study the scriptures of Scientology to the exclusion of all other materials. (Stip. Rec. II 206, 219, 225-26, 229.) As part of training, a person may audit others. (Stip. Rec. I 19-20, 112, 140; II 219, 222). The purpose of undergoing training is to achieve religious enlightenment and the ability to help others (including the ability to audit another person). Dr. Love gave uncontradicted expert testimony that "training" is a form of religious observance comparable to devotional study of sacred texts in the Buddhist and Judaic traditions (Stip. Rec. III 400-404). Scientologists believe that the spiritual benefits and awareness derived from auditing and training accrue not only to the individual but also extend to the public at large. (Stip. Rec. 213-14, 223, 238, 260-61, 274-75, 298).

In accordance with those stipulations and testimony, the Tax Court found the practices at issue to be religious. *Graham v. Commissioner*, 83 T.C. at 580 (Pet. App. 18a) ("[P]etitioners wanted to receive the benefit of various religious services provided by the Church of Scientology").

Contrary to the impression that the government attempts to create in its petition, there is no issue in this case concerning the appropriateness of the behavior or operations of the churches and missions that received the payments at issue here. The parties stipulated that Scientology, the faith whose sacraments are at issue here is a religion (10a, ¶ 52) and that the recipients of the contributions, the relevant Scientology missions and churches, were, at all relevant times, churches within the meaning of Internal Revenue Code § 170(b)(1)(A)(i) and tax-

exempt religious organizations under § 501(c)(3) of the Code eligible to receive contributions deductible under § 170. (10a, ¶ 53).

These stipulations mean that, as a § 501(c)(3) organization, each Scientology church that received the donations at issue here "engages primarily in activities which accomplish one or more of [the] exempt purposes specified in Section 501(c)(3), [and no] more than an insubstantial part of its activities is not in furtherance of an exempt purpose." Treas. Reg. § 501(c)(3)-1(c)(1). The stipulations indicate that the exempt charitable purpose of Scientology is the "advancement of religion." Treas. Reg. § 501(c)(3)-1(d)(2). Thus, the stipulations here contradict the government's recitation of factual findings of the Tax Court in a completely separate case that one church of this religion was not eligible for tax exemption in the early 1970s. *See Church of Scientology of California v. Commissioner*, 83 T.C. 381 (1984), *aff'd*, 823 F.2d 1310 (1987), Pet. at 4. The government's recitation regarding that case is, at best, irrelevant.

The Churches of Scientology have established charges for auditing and training and refer to the payments of such charges as "fixed donations" or "fixed contributions." (6a, ¶ 36). Such fixed donations are the payments at issue here. (7a, ¶ 40). Auditing is given in sessions. An "Intensive" is a specific number of hours—12½ or 25—of Auditing intended to be given over a short period of time. (4a, ¶ 21). Fixed donations are sometimes made for an Intensive of 12½ or 25 hours of Auditing. (6a, ¶ 37). These donations, which are based upon a religious tenet of Scientology called the Doctrine of Exchange, constitute the source of most of the funds of the Churches of Scientology and are used to pay the costs of church operations and activities.[3] (6-7a, ¶ 39). *See also* (Stip.

[3] The Doctrine of Exchange is based upon early writings of the Founder of the Church of Scientology concerning the need to bal-

Rec. II 244-47, 294-95). Like the traditional tithe, amounts of fixed donations have been set historically at levels that correspond roughly to a percentage of the income of church members. For example, the Tax Court below found that the fixed donations for 25 hours of auditing has historically been set at the equivalent of three months' pay for average middle class church members. *Graham*, 83 T.C. at 578, n.7 (Pet. App. 15a).

The taxpayers in the test cases testified that they had made their payments so that they or their children could participate in religious services. (Stip. Rec. II 261-62, 308-04; III 355-56.) They also made their payments because they wanted to support the religious goals and projects of their church. (Stip. Rec. II 261-62, 303; III 355.) None of the taxpayers in the designated cases tried below nor the respondents here received any material goods or secular services with respect to the payments at issue.

The Commissioner's position in this case is that payments by individuals to participate in the religious sacraments of their church may be disallowed depending on the form of such payment and the nature and value of the religious service provided. The Tax Court agreed, but the Eighth Circuit reversed.

The Eighth Circuit held that respondents' payments for religious services were deductible. The court held

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ance inflow and outflow (or, put another way, the need to give as well as receive.) (Stip. Rec. II 244-45, 297-98). A person must outflow to maintain a balance and to be an ethical Scientologist. (Stip. Rec. II 297-98). A person who receives but does not contribute or exchange something in kind will suffer spiritual decline. (Stip. Rec. II, 244, 297-98). The Doctrine of Exchange operates in many personal realms of a Scientologist's life, including, for example, relationships and responsibilities with respect to one's children or community, in addition to providing the doctrinal basis for fixed donations. (Stip. Rec. II 297-98). This is not at all dissimilar to the doctrine shared by most Christian churches that to give is Catholic to the soul and makes one whole spiritually.

that under IRS rulings, court opinions, and the legislative history of § 170, the receipt of religious services is not the type of "material, financial or economic benefit" for which a deduction may be disallowed. The court observed that benefits from receipt of religious services are considered as a matter of law primarily to benefit the general public and only incidentally to benefit the individual participants. The court stated that:

> Religious observances of any faith are considered under the law of charity to be of spiritual benefit to the general public as well as to members of the individual faith, with the private benefit to the individual participants being merely incidental to the broader good that is served. . . . *The public benefit from religion remains and predominates regardless of whether church doctrines provide for traditional congregational worship or individual worship as in Scientology or whether donations are voluntary or fixed.*
>
> * * * * [R]egardless of the timing of the payment or details of the church's methods of soliciting contributions from its members, an amount remitted to a qualified church with no return other than participation in strictly spiritual and doctrinal religious practices is a contribution within the meaning of section 170.

821 F.2d at 1326-1327 (emphasis added).

The Eighth Circuit opinion in the instant case explicitly considered and rejected the holding and reasoning of the First Circuit in *Hernandez v. Commissioner*, 819 F.2d 1212 (4th Cir. 1987), a case affirming the same Tax Court decision based on the same record.

In addition to the First Circuit's decision in *Hernandez*, two other courts of appeals have affirmed the decision of the Tax Court in the test case. *Miller v. Internal Revenue Service*, 829 F.2d 500 (4th Cir. 1987), *petition for cert. filed*, March 1, 1988 (No. 87-1449); *Graham v. Commissioner*, 822 F.2d 844 (9th Cir. 1987).

DISCUSSION

1. In its petition for certiorari, the government observed that if the "conflicting holdings" among the courts of appeals in these cases are permitted to stand "disparate tax treatment for similarly situated taxpayers" will result. Pet. at 6-7. The government's petition also commented on the number of individual cases directly at issue: "[t]here are more than 1,000 taxpayers" with cases currently pending and "there are likely to be more in the future." *Id.* at 7. The government also emphasized the important conflicts in the decisions in the courts of appeals on the "validity of the legal proposiiton" at issue here and in particular, over the applicability to religious services of this Court's holding in *United States v. American Bar Endowment*, 477 U.S. 105 (1986), which denied charitable contribution deductions for payments to purchase life insurance. *Id.* at 7, 8. The government concluded that "resolution by this Court of the conflict in the circuits on the question presented here would be appropriate." *Id.* at 9. Respondents agree with these statements and do not oppose the petition for a writ of certiorari.

2. In *Hernandez v. Commission*, 819 F.2d 1212, a case based on the same Tax Court record as the instant case, the taxpayer, represented by the undersigned, filed his petition for certiorari in this Court on December 11, 1987. No. 87-963. That petition, like the government's petition in the instant case, observed that the direct conflict among the circuits here, coupled with the exceptional importance of the issues presented, warranted plenary review by this Court.

In addition, the taxpayer's petition in *Hernandez* explained why we believe that the panel of the First Circuit incorrectly resolved the legal issue before it, noting: (1) that the Tax Court's decision improperly reverses

nearly seven decades of consistent IRS practices (*Hernandez* Pet. No. 87-963 at 12); (2) that the decision grants the IRS a license selectively to disallow individuals' deductions for payments made to their churches solely to participate in the religious services of their faith (*Id.* at 15); (3) that the decision misreads and improperly extends the 1986 decision of this Court in *United States v. American Bar Endowment*, 477 U.S. 105, to require IRS valuation of religious services—a task that is both impractical and unconstitutional (*Id.* at 21); and (4) that the denial of charitable contribution deductions under § 170 for auditing by Scientologists violates the religion clauses of the first amendment (*Id.* at 25). By reversing the Tax Court's decision and holding that the receipt of religious services cannot constitute the kind of "material, financial or economic benefit" that can serve to disallow charitable deductions, the Eighth Circuit avoided each of these difficulties. We therefore disagree with petitioner's contention that the court of appeals erred in holding that payments made by individuals to solely to participate in for religious services must always be treated as deductible contributions under § 170.

3. Counsel for respondents has filed with this Court two petitions for certiorari on behalf of taxpayers in cases based on records identical to that of the instant case and raising the same legal issues. *Hernandez v. Commissioner*, 819 F.2d 1212 (1st Cir. 1987), *petition for cert. filed*, Dec. 11, 1987 (No. 87-963) and *Miller v. Internal Revenue Service*, 829 F.2d 500 (4th Cir. 1987), *petition for cert. filed*, March 1, 1988 (No. 87-1449). Counsel intends to file a petition with this Court in a third such related case on or before March 30, 1988. *Graham v. Commissioner*, 822 F.2d 844 (9th Cir. 1987), Order Extending Time To File Petition For Writ Of Certiorari until March 30, 1988, entered February 19, 1988 (No. A-640) (O'Connor, Circuit Justice).

In each of these three cases, in addition to holding that § 170 of the Internal Revenue Code requires dis-

allowance of the deductions at issue here, the courts of appeals rejected the taxpayers' contentions that the Commissioner's interpretations of § 170 of the Internal Revenue Code violate the religion clauses of the first amendment. A decision in favor of the government on the statutory issues involved in this case necessarily raises substantial constitutioial questions under the first amendment. In the instant case, the Eighth Circuit found it unnecessary to address the constitutional issues because of its holding that respondents' payments to their church for participation in strictly religious practices were deductible contributions within the meaning of § 170. 821 F.2d at 1328, Pet. App. 9a.

The government's petition in this case does not present the constitutional question, but in other papers filed with this Court in a related case, the government suggests that the statutory issue can be addressed apart from the constitutional issue. *See* Brief for Respondent on Petition for a Writ of Certiorari in *Hernandez v. Commissioner*, No. 87-963 at 8-9 (not opposing taxpayer's petition on statutory grounds, but suggesting no review of the constitutional issue). To the contrary, Congress' special consideration of religion and churches throughout the Internal Revenue Code is in response to first amendment concerns. *See, e.g.*, 26 U.S.C. § 7611 (relating to restrictions on church tax inquiries and examinations). Indeed, special concern for entanglement with churches seems to account for the sharp distinction in IRS policy, heretofore consistently followed, between allowing without question deductions for membership dues to churches and synagogues and reducing deductions for membership dues to secular organizations by the value of secular benefits made available to members. *Compare* Rev. Rul. 70-47, 1970-1 C.B. 49 (reaffirming A.R.M. 2, 1 C.B. 150 (1919)) with Rev. Rul. 68-432, 1968-1 C.B. 104. First amendment issues are inextricably intertwined with the statutory questions at issue here. To take but one addi-

tional example, in *Hernandez v. Commissioner*, 819 F.2d 1212, 1217 (1987), the First Circuit offered three methods for valuing the religious services which are at issue here: by looking "either to (1) the price set by the service providers, (2) the prices set by providers of similar services, or (3) the costs of providing the services." In addition to the practical difficulties that such valuation poses, these valuation methods face constitutional obstacles. For example, the very notion of comparing relative values of religious services or determining allowable charitable deductions based on the costs to a church of providing religious sacraments would violate first amendment prohibitions on entanglement of church and state both through the valuation of religious services and the creation of denominational preferences. *See Walz v. Tax Commissioner*, 397 U.S. 664, 674 (1970); *Larson v. Valente*, 456 U.S. 228, 234 (1982).

In addition, the circuit courts that have affrmed the Tax Court's decision have misapplied this Court's holdings regarding the protections of the first amendment in *Bob Jones University v. United States*, 461 U.S. 574, 603-04 (1983) and in *United States v. Lee*, 455 U.S. 252 (1982). These courts of appeals have failed to recognize that the disallowance of a tax deduction for payments solely to participate in religious sacraments imposes a burden on taxpayers' religious practices by subjecting them to income tax, which burden requires the government to demonstrate both that a compelling state interest exists for its actions and that no less restrictive alternative is available. *Bob Jones University v. United States*, 461 U.S. at 603-04.

In addition, the three affirming courts of appeals have accepted without question the IRS's contention that a compelling state interest exists here in the need to maintain a sound and uniform tax system. Although the *Lee* case, 455 U.S. 252, establishes that the need for a sound and uniform tax system can satisfy the government's

burden of showing a compelling state interest, that case does not give the government a license simply to assert that any interpretation of the tax law automatically satisfies its constitutional burden. The IRS practice—consistently followed from the publication of A.R.M. 2, 1 C.B. 150, in 1919 until the inception of this litigation—of allowing charitable deductions for payments for religious services, regardless of their form or nature or value, has provided sound tax administration for seven decades; there is no compelling state interest for the rule being advanced by the government here.

Finally, the distinction drawn by the affirming courts of appeals in these cases between the individual worship of Scientologists and the congregational worship of other religious faiths creates a denominational preference in violation of the Establishment Clause. The first amendment simply does not permit the government's construction of this statute under which deductions would be allowed for payments for congregational worship, regardless of the form of payment, but deductions would be disallowed for Scientologists' payments to participate in the individual worship of their faith. *Larson v. Valente*, 456 U.S. 228, 244 (1982); *Everson v. Board of Education*, 330 U.S. 1, 15 (1947).

In addition to the important issue of statutory interpretation of § 170 of the Internal Revenue Code presented by this case, therefore, significant first amendment issues are raised by the opinions of the three courts of appeals that have affirmed the Tax Court decision. In addition, the special constitutional status of religion is directly relevant to the interpretation of § 170 at issue here. If review of the decision below is granted, a fair hearing requires that this Court's review should also include review of the important constitutional issues necessarily raised by the decisions of those courts of appeals directly contrary to the decision below.

4. In its petition in the instant case, the government indicated that "if possible," it "would be preferable for this Court to consider the question presented here" in the *Graham* case, and has indicated that it does "not intend to oppose" the taxpayer's petition in that case. Pet. at 9. The government asserts that in *Graham*, "a concrete factual context" exists. *Id.* The basis for the government's preference for the *Graham* case is mysterious. Since the entirety of the record in *Graham*, was stipulated to be part of the record in the instant case, as well as to be included in the record in the *Hernandez* and *Miller* cases, there is nothing in the *Graham* record that was not before the courts of appeals in these other cases and nothing that would not be before this Court if it grants review in any of these cases. Moreover, a case and controversy is equally present between the taxpayers and the government in each of these cases and each case raises identical legal issues.

There are a variety of alternatives that the Court might pursue in reviewing one or more of these related cases. For example, the Court could grant review in each of the related cases and consolidate them for argument; since counsel in this case represents all the taxpayers in each of these cases, such consolidation would not require any additional time for argument or briefing by the taxpayers or the government. Alternatively, the Court may wish to grant the taxpayer's petition in *Hernandez*, the first case before the Court, and hold the petition in the instant case and other related cases pending disposition of *Hernandez*. With three petitions having been filed, both by taxpayers and by the government, there seems little reason to delay resolution of these important issues while awaiting the filing of a fourth petition based upon the identical Tax Court record.

CONCLUSION

The pending petition for a writ of certiorari in this case should be disposed of as appropriate in light of the pending petitions of certiorari in *Hernandez v. Commissioner*, No. 87-963 and in *Miller v. Commissioner*, No. 87-1449.

Respectfully submitted,

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March, 1988

APPENDICES

APPENDIX A

UNITED STATES TAX COURT

Docket No. 5837-76

KATHERINE JEAN GRAHAM,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

[Filed Dec. 6, 1982]

STIPULATION #1

In accordance with Tax Court Rule 91, the parties hereby stipulate the matters hereinafter stated, subject to the rights of the parties to introduce other and further evidence not inconsistent herewith and reserving to each of the parties the right to object to the materiality or relevance hereof in whole or in part.

1. Petitioner maintained her legal residence at 743 Pumehana, Hawaii, at the time of the filing of the petition herein.

2. Petitioner filed a timely Federal Income Tax return for the taxable year ending December 31, 1972, a true and correct copy of which is attached hereto and marked as Joint Exhibit 1-A.

3. Petitioner's income tax return for said taxable year was examined by respondent, who, on April 7, 1976, is-

sued a notice of deficiency, a true and correct copy of which is attached hereto and marked as Joint Exhibit 2-B.

4. Petitioner claimed a charitable contribution deduction under I.R.C. § 170 for $2,379.50 transferred to the Church of Scientology of Hawaii and to the Scientology and Dianetic Center of Hawaii.

5. Each of Exhibits C through Q is a document received by petitioner from the Church of Scientology of Hawaii or from the Scientology and Dianetics Center for Hawaii, reflecting transactions of petitioner with one or the other of them.

6. During November of 1972, petitioner paid $200.00 to the Church of Scientology of Hawaii for Auditing, which payment is not reflected on respondent's Exhibits C through Q.

7. The neologisms "Scientology" and "Dianetics" were introduced by L. Ron Hubbard. Mr. Hubbard wrote *Dianetics: The Modern Science of Mental Health*, which was published in 1950 and which sets forth the general principles of Dianetics and Dianetic Auditing as discovered and developed to 1950.

8. Some of the beliefs and practices of Scientology are roughly described in lay terms in *Scientology, A World Religion Emerges in the Space Age*, a book copyrighted by L. Ron Hubbard. Respondent's Exhibit R attached hereto is a true copy of said book. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

9. The Church of Scientology of Hawaii is, and is considered by the Churches of Scientology to be, a church of the kind referred to by Scientologists as a "Class IV Church" or "Class IV Org." The Scientology and Dianetics Center of Hawaii is, and is considered by Churches

of Scientology to be, a church of the kind referred to by Scientologists as a "Mission."

10. There are many churches and missions in the United States and in other countries which practice, teach and promulgate Scientology. As used herein, "Churches of Scientology" refers collectively to such churches and missions, and "Scientologist" refers to members of such churches and missions.

11. The Churches of Scientology, including the Church of Scientology of Hawaii and the Scientology and Dianetics Center of Hawaii, follow common doctrines, practices and beliefs of Scientology.

12. The Churches of Scientology offer Auditing and courses to Scientologists.

13. Auditing, also variously referred to as "processing," "counselling" and "pastorial counselling," is conducted by a specially trained Scientologist, referred to as an "Auditor."

14. Auditing is generally conducted in a private session one to one, between the Auditor and the person being Audited.

15. Every Auditing session is structured and conducted in exact accordance with rituals, codes, doctrines and tenets of Scientology.

16. Scientologists are taught that the individual is an immortal spirit who has a mind and a body. Scientologists are also taught that the highest level of spiritual ability and awareness can be attained only by progressing on a step by step basis through lower and intermediate levels of Auditing.

17. The structure, ritual and content of each Auditing session are determined by the level of attainment of the Scientologist being Audited.

18. Some of the rituals used in Auditing include questions, commands and drills.

19. The Auditor acknowledges the response of the person being Audited, but offers no analysis of the response to the person being Audited.

20. An E-Meter is a device used in Auditing.

21. Auditing is delivered in sessions. An "Intensive" is a specific number of hours of Auditing intended to be given over a short period of time. An intensive is 12½ or 25 hours of Auditing and usually involves 12½ hours of Auditing.

22. An Auditor who conducts a session is expected to know and understand the rituals, codes, tenets and doctrines of Scientology applicable to the conduct of Auditing generally and to have mastered the particular material to be used in the session.

23. No subject matter is taught, studied or learned during an Auditing session (except that the Scientologist being Audited necessarily learns and understands the particular practice used in the session).

24. The Churches of Scientology offer courses to provide training in the doctrines, tenets, codes, policies and practices of Scientology and to train Scientologists as Auditors.

25. Training is delivered to Scientologists under the supervision of a trained Scientologist. Training is delivered in courses each of which includes specific material to be mastered by the students in order to complete the course. Courses range from basic courses which introduce the doctrines and tenets of Scientology through courses which train and qualify Auditors to deliver Auditing at the highest levels.

26. It is a doctrine of Scientology, and Scientologists are taught, that spiritual gains result from the study and understanding of the doctrines, codes and tenets of Scientology, whether or not the student receives Auditing.

27. Scientologists believe that they can attain benefits from Auditing, but only in degrees or steps. These include levels called "Grades" and higher levels called "OT Sections."

28. Respondent's Exhibit S attached hereto is a copy of a document headed "THE BRIDGE" which was published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

29. In contrast to Auditing, Auditor training and other courses furnished by the Churches of Scientology are instructional or educational; the student is expected to understand and learn the material which is the subject matter of the particular course he or she takes. As used herein, "course" means and refers to such services and not to Auditing. Some courses including Auditing by students and Auditing of students.

30. The Churches of Scientology deliver Auditing and training at various levels. A Scientologist who receives Auditing begins at the lowest level and progresses step by step to higher and higher levels. A Scientologist who receives training also begins at the lowest level and progresses step by step to higher and higher levels. Only Auditors who have been qualified by training at an appropriate level can deliver Auditing at that level.

31. Some of the Churches of Scientology also deliver administrator and executive training courses. The students in such courses are taught the management methods and policies of the Churches of Scientology, and are mostly staff members of the Churches of Scientology.

Such courses are occasionally taken by Scientologists who are not staff members. The subject matter of such courses includes Scientology doctrines, tenets and codes which are applicable to the administration and management of Scientology organizations.

32. The Churches of Scientology also deliver a few short courses of a general educational nature, designed to remedy educational deficiencies and to teach Scientology study methods, to enable the student to progress more rapidly in Scientology courses.

33. All of the courses offered by the Churches of Scientology are founded upon the doctrines and tenets of Scientology, in the manner of presenting the material studied and in the instructional methods.

34. The Scientology and Dianetic Center of Hawaii offers Auditing at Grades I through IV.

35. The Church of Scientology of Hawaii offer Auditing from Grade I through Grade IV and Auditor training from Class I through Class IV.

36. The Churches of Scientology have established charges for Auditing and for courses they deliver, and refer to payments of such charges as "fixed donations" or "fixed contributions." Such payments are hereinafter referred to as "fixed donations."

37. Fixed donations are sometimes made for an Intensive 12½ or 25 hours of Auditing.

38. Respondent's Exhibit T attached hereto is a copy of a schedule of fixed donations and book order form, copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

39. Fixed donations constitute the source of most of the funds of the Churches of Scientology. Their only

other source of funds is from sales of Scientology literature, tapes of lectures by L. Ron Hubbard (the founder of Scientology) and artifacts.

40. The payments made by petitioner were fixed donations.

41. The Churches of Scientology do not actively solicit contributions from their members or from the public, other than fixed donations.

42. Petitioner first became a Scientologist in 1971 when she attended activities of the Scientology and Dianetics Center of Hawaii.

43. The Hubbard Qualified Scientologist Course (HQS) is an introductory course, one purpose of which is to familiarize the student with certain basic techniques used in Auditing.

44. Respondent's Exhibit U attached hereto is a copy of a pamphlet copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

45. The Communications Course is an introductory course one purpose of which is to introduce those unfamiliar with Scientology to certain concepts of Scientology.

46. Respondent's Exhibit V attached hereto is a copy of a pamphlet copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

47. The Communications Course referred to in respondent's Exhibit H was attended by petitioner's daughter, Karen.

48. The Communications Course referred to in respondent's Exhibit I was attended by petitioner's daughter, Laurel.

49. The Hubbard Qualified Scientologist Course referred to in respondent's Exhibit J was attended by petitioner's daughter, Karen.

50. The Hubbard Qualified Scientologist Course referred to in respondent's Exhibit K was attended by petitioner's daughter, Laurel.

51. Respondent's Exhibits W through AQ attached hereto are copies of documents, each of which was published and/or copyrighted as follows:

W Two page flyer, first page headed "Knowledge Services—Books," published by ASHO (Church of Scientology of California) and copyrighted by L. Ron Hubbard.

X Booklet entitled "Scientology & Dianetics," published by Church of Scientology of California.

Y Magazine, the cover of which is missing, published by the Founding Church of Scientology of Washington, D.C. and commencing with an article entitled "The Dangerous Environment."

Z Booklet entitled "Church of Scientology Information, Definitions, Rules," copyrighted by L. Ron Hubbard.

AA Flyer entitled "Gain Respect for Self and Others Through Scientology Training," published by the Los Angeles Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AB Flyer entitled "Your Road to Total Freedom," published by Church of Scientology of California and copyrighted by L. Ron Hubbard.

AC Flyer commencing with excerpts titled "On Exchange," published by the San Francisco Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AD Flyer entitled "Scientology Auditing gives you a chance to handle your environment better," published by The Church of Scientology Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AE Booklet entitled "Your Road to Clear Goes Through ASHO Foundation," published by Church of Scientology of California and copyrighted by L. Ron Hubbard.

AF Magazine entitled "Advance," Issue 18, published by the Advanced Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AG Magazine entitled "Advance," Issue 19, published by the Advanced Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AH Magazine entitled "Gateway," Issue 61, published by the Church of Scientology in San Francisco (Church of Scientology of California) and copyright by L. Ron Hubbard and copyright by L. Ron Hubbard.

AI Magazine entitled "Gateway," Issue 73, published by the Church of Scientology in San Francisco (Church of Scientology of California).

AJ Magazine entitled "THE AUDITOR: The Monthly Journal of Scientology," Issue 92 Worldwide, published by New American Saint Hill Organization (Church of Scientology of California) and copyright by L. Ron Hubbard and copyright by L. Ron Hubbard.

AK Magazine entitled "THE AUDITOR: The Monthly Journal of Scientology," Issue 91 Worldwide, published by New American Saint

Hill Organization (Church of Scientology of California).

AL Magazine entitled "Cause," Issue 26, published by ASHO Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AM Magazine entitled "Cause," Issue 26, published by ASHO Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AN Magazine entitled "Clear News," Issue 107, published by AOLA (Advanced Organization, Los Angeles—Church of Scientology of California) and copyright by L. Ron Hubbard.

AO Magazine entitled "Clear News," Issue 104, published by AOLA (Advanced Organization, Los Angeles—Church of Scientology of California) and copyright by L. Ron Hubbard.

AP Magazine entitled "Realty," Major Issue 96, published by Church of Scientology of California and copyright by L. Ron Hubbard.

AQ Magazine entitled "Realty," Issue 102, published by Church of Scientology of California.

Petitioner objects to each of said exhibits on grounds of relevance, hearsay and the first amendment.

52. Respondent has not contested and will not contest, but only for the purposes of this litigation, petitioner's contention that Scientology was at all relevant times a religion.

53. Respondent has not contested and will not contest, but only for the purposes of this litigation, petitioner's contention that each Scientology organization to which petitioner paid money was at all relevant times a church within the meaning of I.R.C. § 170(b)(1)(A)(i), a corporation described in I.R.C. § 170(c)(2) and exempt

from general income taxation under I.R.C. § 501(a) as an organization described I.R.C. § 501(c)(3).

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APPENDIX B

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

First Amendment

Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof . . . .

Internal Revenue Code of 1954 (26 U.S.C.) § 170—Charitable, etc., Contributions and Gifts *

(a) Allowance of deduction.

(1) General rule. There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. * * *

(b) Percentage limitations.

(1) Individuals.—In the case of an individual, the deduction in subsection (a) shall be limited as provided in the succeeding subparagraphs.

(A) General rule. Any charitable contribution to—

(i) a church or a convention or association of churches.

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* Only those portions of 26 U.S.C. § 170 and 26 U.S.C. § 501 relevant to the discussion in this petition are set forth here. References to Title 26 United States Code are to the Internal Revenue Code of 1954, which was in effect when the tax returns at issue in this case and related cases were filed and when the Commissioner's notices of deficiency were issued. As part of the Tax Reform Act of 1986, the 1954 Code was redesignated the Internal Revenue Code of 1986. Pub. L. 99-514 § 2(a), 100 Stat. 2085, 2095. The portions of sections 170 and 501 of the 1954 Code pertinent to this case were not changed by the Tax Reform Act of 1986 and remain in force in identical form.

shall be allowed to the extent that the aggregate of such contributions does not exceed 50 percent of the taxpayer's contribution base for the taxable year.

(c) Charitable contribution defined. For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of:

* * * *

(2) A corporation, trust, or community chest, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if it is to be used within the United States or any of its possessions exclusively for purposes specified in subparagraph (B).

* * * *

Internal Revenue Code of 1954 (26 U.S.C.)
§ 501—Exemption From Tax on Corporations, Certain Trusts, Etc.

(a) Exemption From Taxation. An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

* * * *

(c) List of Exempt Organizations. The following organizations are referred to in subsection (a):

* * * *

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

* * * *